



DEPARTMENT OF
FINANCE

ARNOLD SCHWARZENEGGER, GOVERNOR

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October 23, 2008

Mr. Glenn Stober, Director
California Business, Transportation, and Housing Agency
980 Ninth Street, Suite 2450
Sacramento, CA 95814

Dear Mr. Stober:

**Final Report—Inland Empire Small Business Financial Development Corporation,
Agreed-Upon Procedures**

The Department of Finance, Office of State Audits and Evaluations (Finance), has completed its agreed-upon procedures review of the Inland Empire Small Business Financial Development Corporation's (Inland Empire) compliance with the Small Business Loan Guarantee Program for the period July 1, 2006 through June 30, 2007.

The enclosed report is for your information and use. Because there were no findings or issues requiring a response, we are issuing this report as final. In accordance with Finance's policy of increased transparency, the final report will be placed on the Finance website.

We appreciate the assistance and cooperation of Inland Empire staff during the review. If you have any questions regarding this report, please contact Kimberly Tarvin, Manager, or Rich Hebert, Supervisor, at (916) 322-2985.

Sincerely,

Original signed by:

David Botelho, Chief
Office of State Audits and Evaluations
(916) 322-2985

Enclosure

cc: Ms. Karen Kawada, Program Analyst, California Business, Transportation, and Housing Agency
Mr. Robert Saenz, President, Inland Empire Small Business Financial Development Corporation

AGREED-UPON PROCEDURES

Inland Empire Small Business Financial
Development Corporation

Small Business Loan Guarantee Program
For the Period July 1, 2006
Through June 30, 2007

Prepared By:
Office of State Audits and Evaluations
Department of Finance

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This report is also available on our website at <http://www.dof.ca.gov>

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INDEPENDENT ACCOUNTANT'S REPORT ON APPLYING AGREED-UPON PROCEDURES

Mr. Glenn Stober, Director
California Business, Transportation, and Housing Agency
980 Ninth Street, Suite 2450
Sacramento, CA 95814

The Department of Finance, Office of State Audits and Evaluations (Finance), performed the procedures enumerated below, which were agreed to by the California Business, Transportation, and Housing Agency (BT&H) to assist in evaluating Inland Empire Small Business Financial Development Corporation's (Inland Empire) compliance with the Small Business Loan Guarantee Program (SBLGP). Inland Empire's management is responsible for compliance with these requirements. This review covers the period July 1, 2006 through June 30, 2007.

This agreed-upon procedures engagement was conducted in accordance with the *Statements on Standards for Attestation Engagements* published by the American Institute of Certified Public Accountants. These standards require that we report all findings identified during the application of the agreed-upon procedures. For findings that include questioned costs, materiality was defined as errors or omissions of \$1,000 or more. The sufficiency of these procedures is solely the responsibility of the BT&H. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

Background

The SBLGP was created by the Legislature to encourage lenders to provide funds to small businesses and farming enterprises that need additional collateralization in the form of a guarantee. The loan guarantees provide the following:

- Encourage the development of small business opportunities for minority, women, and disabled persons.
- Alleviate unemployment.
- Allow participation in state public works contracts by small and emerging contractors.

The SBLGP was established within the California Technology, Trade, and Commerce Agency (CTTCA) and administered by the Office of Small Business Loan Guarantee Program. The CTTCA created a Loan Guarantee Trust Fund (Fund) to collateralize the guarantees on loans to small businesses made by local lending institutions. Under a contractual agreement with the CTTCA, which was subsequently transferred to BT&H, program administration and direction of certain Fund account transactions were assigned to eleven regional financial development

corporations. Each corporation issues guarantees on behalf of the state and manages its share of the Fund and portfolio of outstanding guarantees.

Inland Empire was established in 2001 and is one of the eleven regional financial development corporations. Inland Empire's mission is to create and retain jobs and promote economic development within communities by assisting small businesses to obtain financing through local banks in the greater Inland Empire region of Southern California. During the period July 1 2006 through June 30, 2007, Inland Empire claimed \$286,300, which consists of \$175,000 for personnel and rent costs, and \$111,300 for loan guarantee fees.

Procedures Performed and Results

1. Verification of Allowable Costs

a. Operational Expenses

Inland Empire claimed \$175,000 for operational and administrative costs. To determine whether the costs claimed were allowable as stipulated in the contract, we performed the following procedures:

- Reviewed the grant agreement to identify authorized positions and allowable salary rates.
- Verified personnel expenses claimed were supported by timesheets and paychecks, and that expenses claimed did not exceed the actual salaries paid.
- Analyzed the fringe benefits claimed to ensure that the percentage of personnel expenses claimed did not exceed the allowable rate.
- Verified that rent expenses were supported by the rental agreement and canceled checks.

Based on the procedures performed, the operational and administrative costs claimed were allowable, supported, and in compliance with the terms of the contract.

b. Loan Guarantee Fees

Inland Empire claimed and was paid \$111,300 for guarantee fees based on the issuance of 30 new loans at \$3,250 per loan and 6 renewal loans at \$2,300 per loan. To verify that the loan guarantee fees claimed were allowable, we performed the following procedures:

- Identified the loan guarantees issued from the Monthly Loan Guarantee Registration Report.
- Reviewed a sample of borrower files, including the promissory notes and the Board of Directors and Loan Committee meeting minutes, to confirm the loan was made and determined whether it was a new loan or a renewal.
- Recalculated the variable fees to determine whether the loan guarantee fees were accurately claimed.

Based on the procedures performed, we determined that the loan guarantee fees were accurately claimed and allowable.

2. Contracting Practices

We verified that contracting practices were appropriate by determining whether related-party relationships existed with contractors. Specifically, we performed the following procedures:

- Interviewed Inland Empire staff to gain an understanding of contracting practices.
- Reviewed the Statement of Economic Interest forms completed by Inland Empire staff and officers.
- Determined whether any of Inland Empire staff or officers reported any economic interest in any of the contractors.
- Reviewed the contract agreements and general ledger to identify any transactions that indicate the existence of related-party relationships.

Based on the procedures performed, we did not identify any related-party relationships and determined that Inland Empire's contracting practices are appropriate.

3. Cost Allocation

To determine whether Inland Empire's cost allocation plan methodology was reasonable and appropriately applied, we interviewed staff and reviewed financial records to determine whether Inland Empire had any other programs in addition to the SBLGP that would require allocation of costs between programs.

We determined that Inland Empire only operates the SBLGP program. Therefore, Inland Empire is not required to have a cost allocation plan to distribute costs among programs.

4. Record Maintenance

To verify all required records are maintained, we performed the following:

- Interviewed Inland Empire staff to obtain an understanding regarding the records maintained.
- Reviewed the general ledger, Loan Guarantee Program Database, Loan Committee minutes, loan portfolio records, and contract agreements.

Based on the procedures performed, we determined that Inland Empire maintains the required documents.

5. Collection Costs

We interviewed staff and reviewed the general ledger and the Loan Guarantee Program Database to determine whether:

- Collection costs are charged correctly.
- Out-of-pocket costs were paid for each collection effort with the monies received by a single successful collection.

Based on procedures performed, Inland Empire did not charge collection costs or pay out-of-pocket costs for collection efforts.

6. Timely Deposit of Recovery Funds

To determine the length of time between the receipt of recoveries and when funds are forwarded to the state or trustee for deposit, we interviewed staff and reviewed the Loan and Guarantee Program Database and the general ledger.

Based on the procedures performed, we determined that Inland Empire did not recover any loan defaults during the period under review.

7. Accuracy and Reconciliation of Loan Guarantee Portfolio Records

To determine whether the loan guarantee approval process is adequately documented and whether the portfolio records are accurate and reconcile with bank records, we performed the following procedures:

- Interviewed Inland Empire staff to obtain an understanding of the loan guarantee approval process and records maintained.
- Reviewed a sample of loan guarantee files to evaluate the adequacy of the loan guarantee approval process documentation.
- Reviewed the Loan Guarantee Program Database to determine whether it was updated when an extension was granted to a matured line of credit.
- Determined whether the loan guarantee portfolio records were accurate and reconciled with bank records.

Based on our review, the loan guarantee approval process is adequately documented in the loan guarantee files. Additionally, the Loan Guarantee Program Database is updated when a mature line of credit is granted an extension. Furthermore, Inland Empire receives periodic confirmation reports from lenders on the status of loans and reconciles this information with the Loan Guarantee Program Database. Any variances identified during the reconciliation process are resolved with the lender and reported to BT&H.

8. Monitoring of Collateral Holdings

To determine whether Inland Empire communicates the status of the collateral holdings and to identify Inland Empire's monitoring efforts, we performed the following procedures:

- Interviewed Inland Empire staff to identify communication and monitoring procedures.
- Reviewed lender confirmation reports to determine whether the information is reconciled to the Loan Guarantee Program Database.

Based on the procedures performed, Inland Empire regularly communicates with the lenders, receives quarterly reports on loan status changes, and updates the Loan Guarantee Program Database accordingly.

9. Review of Accounting Procedures

To determine whether Inland Empire's accounting procedures are designed to prevent double billings and ensure the separation of duties are adequate, we performed the following procedures:

- Interviewed Inland Empire staff regarding accounting processes.
- Reviewed the Inland Empire organization chart.

Because Inland Empire did not have an accounting procedures manual, we relied upon Inland Empire's description of its accounting process. Inland Empire uses QuickBooks Pro 2002 to record the accounting transactions. The accounting procedures incorporate separation of duties and are adequately designed to prevent double billing.

10. Review of Independent Auditor's Report

We reviewed the single audit report prepared by Inland Empire's Certified Public Accountant (CPA) for the fiscal periods ending June 30, 2006 and June 30, 2007, and the CPA's working papers to identify internal control weaknesses in the accounting procedures.

Our review of the audit report and working papers did not identify any internal control weaknesses.

We were not engaged to and did not conduct an examination, the objective of which would be the expression of an opinion on compliance with SBLGP requirements. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of BT&H, and is not intended to be and should not be used by anyone other than the specified parties. However, this report is a matter of public record and its distribution is not limited.

Original signed by:

David Botelho, CPA
Chief, Office of State Audits and Evaluations
(916) 322-2985

October 16, 2008